

MEMORANDUM

To: *Payment System Compliance for Credit Unions Customers*

From: Sheshunoff Information Services

Subject: Highlights

The legal, compliance, and operational aspects of payment systems continue to undergo changes as Congress, regulators, and the courts address these areas. Enclosed is the latest update to *Payment System Compliance for Credit Unions*. This update provides new and revised information on the following topics:

- **The FRB issues final amendments to Regulation Z's credit card disclosure requirements.** The product of a multiyear effort, the FRB has completely overhauled the disclosure requirements for credit cards. In Chapter 12, we give a detailed explanation of the new disclosure requirements through the life-cycle of a credit card account.
- **The FRB issues final "unfair practice" rules for credit cards.** In Chapter 12, we also review the new regulations that label several common credit card features as unfair and deceptive acts and practices. These rules are generally effective as of July 1, 2010.
- **Congress adopts The Credit CARD Act of 2009.** Not satisfied with the scope or timing of the FRB's new unfair practices rules for credit cards, Congress adopted new legislation that covers much of the same ground. However, it has a much broader sweep and shorter implementation period. We summarize the Act in Chapter 12.
- **New IAT ACH Rule Takes Effect.** Starting on September 18, 2009, all ODFIs and Gateway Operators must identify all international ACH transactions by using a new IAT standard entry class code. In addition, all IAT entries must include information required by the Bank Secrecy Act's Travel Rule. This will enable all parties to the transaction to comply with U.S. law, particularly the various economic sanctions programs administered by the Office of Foreign Assets Control. We discuss this new requirement in Chapter 14.
- **Supreme Court cuts back on preemption.** In Chapter 3, we analyze the Supreme Court's recent opinion striking down the part of the OCC's preemption regulation that prohibited state attorneys general from bringing judicial enforcement actions against federally chartered financial institutions. This opinion has wide-ranging consequences for the financial services industry and is a green light for state attorneys general to sue industry participants to enforce unfair and deceptive practices statutes and other state laws. It will greatly increase the regulatory burden faced by the financial services industry.
- **Federal regulators issue Guidance on risk management for remote deposit capture.** On January 9, 2009, the Federal Financial Institutions Examinations Council (FFIEC) issued Guidance on how financial institutions should design and implement a risk management program for RDC products. We summarize this new Guidance in Chapter 1.
- **New case law on high-to-low debit posting.** In Chapter 3, we discuss three new judicial decisions that have recently come down on high-to-low debit posting—a contentious issue for consumer advocates. One of the decisions (from New Jersey) protects high-to-low posting, particularly where the institution has clear disclosure of the practice in its account agreement. The other two cases (one

from Georgia, one from California) strike down the practice, at least with respect to certain types of electronic debits.

- **California supreme court okays application of direct social security deposits to satisfy overdrafts.** A recent decision of the California supreme court, anxiously awaited by the financial services industry, holds that financial institutions can apply electronic deposits of social security and other government benefits to reduce overdrafts in the customer's account. The practice does not constitute an illegal "setoff." This decision, analyzed in Chapter 3, gets Bank of America off a potential \$1 billion hook and validates a widespread practice.
- **California court rules that garnishor of deposit account trumps asset-based lender.** What happens if a depository institution has transferred funds to a garnishing creditor before the transfer is discovered by an asset-based lender who claims funds in the account as proceeds of its security interest? The California case, discussed in Chapter 3, holds that the garnishing creditor wins over the secured lender as a protected "transferee" under the UCC.
- **Litigation continues full steam on right of an institution to charge a service fee for non-accountholders to cash its own official checks.** In Chapter 4, we examine a pair of Michigan decisions by the same judge. The first decision allows a national bank to impose such a fee, based on federal preemption. The second case holds that the rules of the UCC forbid such a fee if it is imposed by a state-chartered bank.
- **In a Texas decision, financial institution gets into trouble for having no written policy on verifying drawer signatures.** Except for checks above certain dollar thresholds, most financial institutions don't visually verify signatures on presented checks to prevent forgeries and counterfeits. The courts generally okay this practice, based on the need for automation in the check collection system. But in a recent case from Texas, the court held the institution liable for failing to have a written policy in place clarifying what the threshold is. We critique this case in Chapter 6.
- **The FRB issues final regulations to implement the Unlawful Internet Gambling Enforcement Act.** Financial institutions need to consider whether they are required to establish and implement written policies and procedures to identify and block payments relating to unlawful Internet gambling. These regulations apply to financial institutions that participate in check collection systems, automated clearinghouse systems, card systems (credit, debit, and stored-value), wire transfer systems, and money transfer systems. We discuss these regulations in Chapters 3, 12, 13, 14, 15, and 16. Compliance is mandatory as of December 1, 2009.
- **The FRB proposes opt in/opt out regulations for ATM and debit card overdrafts.** The FRB is continuing a rulemaking process that began in 2008 with respect to regulating the way in which ATM and debit cards access automated overdraft programs. Chapter 13 contains an overview and analysis of the most recent proposal.
- **New FDIC guidance on relationships with payment processors.** In the wake of the OCC's actions against Wachovia relating to its relationship with a payment processor, the FDIC issued guidance that financial institutions should follow in establishing and monitoring relationships with entities that process payments for third parties through their accounts. We provide an analysis of that guidance in Chapter 14 as it relates to the ACH system.
- **New FDIC general counsel opinion on stored-value cards.** In Chapter 16, we discuss the most recent development in the issue of whether stored-value cards are covered by FDIC deposit insurance. Under a new general counsel's opinion, that coverage generally depends on compliance with the so-called "pass-through" insurance rules.
- **Impact of new credit card legislation on stored-value cards.** Although the focus of the new legislation is clearly credit cards, the new law also impacts stored-value cards in important ways. In

Chapter 16, we review how the law affects expiration dates and dormancy fees and how it may lead to coverage of all stored-value cards by Regulation E.

Our goal with *Payment System Compliance for Credit Unions* is to provide you with practical tips and compliance strategies in this rapidly changing area. Please let us know how we are doing. You can call our customer service representatives at 1-800-456-2340. Please visit us online at www.sheshunoff.com.

Sincerely,

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Editor